Craig S. Tyle
Executive Vice President
General Counsel
Franklin Resources, Inc.
One Franklin Parkway
San Mateo, CA 94403-1906
tel 650.312.4161
franklintempleton.com

FRANKLIN TEMPLETON

July 21, 2020

Submitted electronically: https://www.sec.gov/rules/proposed.shtml

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE : File Number S7-07-20; Good Faith Determinations of Fair Value

Dear Ms. Countryman:

I am writing on behalf of Franklin Resources, Inc., a global investment manager that operates under the name Franklin Templeton Investments ("Franklin Templeton"). As of June 30, 2020, Franklin Templeton managed approximately $623 billion in assets, of which over $354 billion constituted investment companies registered with the U.S. Securities and Exchange Commission ("SEC" or the "Commission") under the Investment Company Act of 1940 (the "1940 Act" or the "Act").

Franklin Templeton appreciates the opportunity to comment on the SEC's proposal to adopt new Rule 2a-5 under the 1940 Act (the "Proposed Rule"),[1] which would address the fair valuation responsibilities of registered investment companies' ("Funds") boards and investment advisers. We participated in the development of, and broadly endorse, the comment letter on this Proposed Rule filed by the Investment Company Institute ("ICI") (though not necessarily each of the specific recommendations set forth in that letter).

We view the SEC's proposal as a substantial step forward from the current regulatory framework, which the SEC last comprehensively addressed approximately fifty years ago. We specifically support the Proposed Rule allowing Fund complexes to assign fair value determinations to Fund investment advisers/sub-advisers[2] and the Proposed Rule's effort to make Fund valuation processes consistent with U.S. generally-accepted accounting principles ("U.S. GAAP").[3] We also support the Proposed Rule not requiring board ratifications of fair value determinations that Fund advisers make.[4] At the same time, we have recommendations for enhancements, which are designed to improve the efficiency and effectiveness of the Proposed Rule in a manner consistent with the protection of Fund investors.

Comments on Making the Proposed Rule Less Prescriptive

The Proposed Rule would formalize Fund valuation management programs and identifies numerous specific steps and elements that a valuation management program must include, as set forth below. We believe that a valuation management program should be flexible depending upon the specific Fund's facts and circumstances, while allowing Funds to continue many of the best practices that they have already adopted to fair value portfolio investments.

To help achieve a more "principles-based" program, we believe that the SEC should remove several of the Proposed Rule's requirements, while relaxing certain other requirements, each as further detailed below.

"Valuation Risk". The Proposed Rule would require a Fund's board or adviser to periodically assess any material risks associated with the determination of the fair value of the Fund's investments, including material conflicts of interest, and to manage those identified "valuation risks".[5] Additionally, if the Fund's board assigns the fair value determination to the Fund's adviser under the Proposed Rule, the Proposed Rule would require the Fund's adviser, as part of the periodic board

[1] Good Faith Determinations of Fair Value, Investment Company Act Release No. 33845 (Apr. 21, 2020), 85 Fed. Reg. 28734 (May 13, 2020) ("Release").
[2] Proposed Rule 2a-5(b).
[3] *See* Release at pg. 59.
[4] *See* Release at pgs. 106-07.
[5] Proposed Rule 2a-5(a)(1).

reporting requirement, to include a written assessment of its assessment and management of material "valuation risks", including any material conflicts of interest of the adviser (and any other service providers).[6]

We believe the references to "valuation risk" are an unnecessary complication that would contribute nothing to investor protection but impose superfluous burdens on Fund boards and those entities to which the boards assign valuation responsibilities. Accordingly, we believe that the SEC should delete both of these requirements from the final rule, as well as other references in the Proposed Rule to "valuation risk".[7] Section 2(a)(41) of the 1940 Act requires Funds to value their portfolio investments (i) using market value when market quotations for those investments are "readily available," and (ii) when a market quotation for a portfolio investment is not readily available, by using "fair value as determined in good faith by the board of directors." The valuation standards under the Act exist independently of any risk assessment, and it is difficult to ascertain how the Commission expects such risk assessments to impact the valuation procedures adopted by a Fund. The examples in the Release only add confusion. For example, let's assume that the value of a particular portfolio security might be disproportionately impacted by "potential market or sector shocks or dislocations." Is the Commission suggesting that the Fund's valuation methods should somehow anticipate this price effect and discount the value? Presumably not, for obvious reasons – but then how is this "risk" relevant? The same is true of "the proportion of the Fund's investments that are fair valued" – is a Fund supposed to value securities differently according to their relative proportion of the overall portfolio? Again, the question answers itself.

The "valuation risk" factor thus amounts to little more than a paper exercise, one which would require the preparation of epiphenomenal written assessments that would not impact valuation methodologies. Worse, under the proposed reporting timelines (discussed further below), these would have to be provided quarterly and, in some cases, perhaps daily.[8] For these reasons, we recommend that it be deleted.

Fair Value Methodologies. The Proposed Rule would provide that fair value as determined in good faith requires selecting and applying in a consistent manner an appropriate methodology or methodologies for determining (which includes calculating) the fair value of Fund investments.[9] We believe that the SEC should remove the "consistency" references from the Proposed Rule as it does not reflect current market practice and could have a negative effect on Funds and Fund investors. For instance, an adviser should be able to apply different methodologies to the same investment over time (e.g., a private equity investment depending upon its "life-cycle stage," or a bond that has had a change in credit rating).

Testing of Fair Value Methodologies. In addition to requiring that boards/advisers select and apply fair value methodologies, the Proposed Rule would require that Funds test the appropriateness and accuracy of the methodologies used to calculate fair value, and to identify (1) the testing methods to be used, and (2) the minimum frequency of the testing.[10] While we believe that testing is a useful and beneficial tool for a fair valuation management program, we also believe that it can be difficult to test fair value methodologies in a vacuum (i.e., without a triggering event to prompt such testing). As such, we do not believe that prescriptive requirements to identify the testing methods to be used for Fund methodologies and the minimum frequency of such testing in advance is appropriate and that the SEC should instead allow for the Funds and their boards to determine in their discretion how testing should be conducted based on the specific Fund's facts and circumstances.

Comments on the Proposed Rule's Treatment of Pricing Services

We believe that the Proposed Rule does not adequately reflect the role that pricing services play in Fund valuation. Funds generally rely on pricing services to perform fair valuation, subject to oversight. Certain aspects of the Proposed Rule – in particular, the proposed recordkeeping requirements – do not take this into account. For example, under the Proposed Rule, Funds would be required to maintain documentation including "information regarding the specific methodologies applied and the assumptions and inputs considered when making fair value determinations." Funds that rely on pricing services would not, and should not be expected to, have written records of this level of detail.

---

[6] Proposed Rule 2a-5(b)(1)(i)(A).

[7] We note that Proposed Rule 2a-5(a)(2) also references "taking into account the fund's valuation risks." We believe such reference should be deleted from the final rule.

[8] As the ICI notes in its comment letter, because material changes in valuation risks would require "prompt" reporting, such reporting could be an ongoing requirement in stressed markets, such as those that existed earlier this year.

[9] Proposed Rule 2a-5(a)(2).

[10] Proposed Rule 2a-5(a)(3).

We therefore recommend that the Proposed Rule be revised to only require Funds to maintain these types of records when the Fund adviser (or other entity that has been assigned fair value responsibilities by the board) is using its own fair value methodologies. Where a pricing service is used, the required records should consist of the prices received, any adjustments made to them and the basis for any such adjustments.

Comments on Assigning Fair Valuation Determinations

The Proposed Rule states that a Fund's board may assign fair valuation to the Fund's investment adviser, or one or more sub-advisers.[11] While we support the Proposed Rule allowing boards to assign fair valuation responsibilities to advisers and sub-advisers, we believe that the SEC should expand the parties to whom boards can assign fair value determinations to include affiliates of the adviser (e.g., Fund administrators or valuation committees comprised of individuals from such affiliated entities). We would recommend that the SEC incorporate a concept similar to the "program administrator" under Rule 22e-4 under the 1940 Act (the "Liquidity Rule"), which allows Funds to approve officers that are appropriate to assume the administrator responsibilities.[12]

Comments on Board Reporting

Periodic Board Reporting: Under the Proposed Rule, if the board assigns fair valuation determinations to the adviser, the adviser would be required, at least quarterly, to provide a written assessment of the adequacy and effectiveness of the adviser's process for determining fair value.[13] Rather than the Proposed Rule's quarterly reports, we believe that an annual program review, similar to that required under the Liquidity Rule, would be more valuable and practicable for Fund boards, while still providing appropriate protection to Fund investors. Many elements of the periodic reports in the Proposed Rule are unlikely to change on a quarterly basis (e.g., valuation risks and the adequacy of the adviser's resources). We believe that requiring a quarterly assessment would impose an unnecessary burden on advisers without providing additional benefits to Fund boards and Fund investors. We would also note that the Proposed Rule should require these assessments annually, "at a minimum," which would allow boards to require more frequent reporting as they deem necessary.

Price Overrides. The Proposed Rule would require that all price overrides be included as part of the Proposed Rule's periodic board reports.[14] We believe that providing a list of price overrides is not a meaningful reporting metric and instead suggest that Funds provide a qualitative discussion of price overrides as part of the annual board program review.

* * * * *

We appreciate the SEC's consideration of our comments and would be pleased to respond to any questions from the SEC or the staff.

Very truly yours,

DocuSigned by:

Craig Tyle

135465427981480...

Craig S. Tyle

---

[11] Proposed Rule 2a-5(b).

[12] *See* Rule 22e-4(a)(13) ("Person(s) designated to administer the program means the fund or In-Kind ETF's investment adviser, officer, or officers (which may not be solely portfolio managers of the fund or In-Kind ETF) responsible for administering the program and its policies and procedures…").

[13] These written assessments would be required to include, at a minimum: a summary/description of: the assessment and management of material valuation risks, including any material conflicts of interest of the investment adviser (and any other service provider); any material changes to, or material deviations from, the fair value methodologies; the results of the testing of fair value methodologies; the adequacy of resources allocated to the process for determining the fair value of assigned investments, including any material changes to the roles or functions of the persons responsible for determining fair value; any material changes to the adviser's process for selecting and overseeing pricing services, as well as material events related to the adviser's oversight of pricing services (such as changes in the service providers used or price overrides); and; any other materials requested by the board related to the adviser's process for determining the fair value of assigned investments. Proposed Rule 2a-5(b)(1)(i).

[14] Proposed Rule 2a-5(b)(1)(i)(E).

cc: The Honorable Jay Clayton
The Honorable Allison Herren Lee
The Honorable Hester M. Peirce
The Honorable Elad L. Roisman

Dalia O. Blass, Director, Division of Investment Management